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DEPT FOR A/S FRAZER, SE WILLIAMSON, AF/SPG, AND EEB/IFD
NSC FOR PITTMAN AND HUDSON
ADDIS ABABA FOR USAU
DEPT PLS PASS USAID FOR AFR/SUDAN
DEPT PLS PASS TREASURY FOR OIA, USED IMF AND USED WORLD BANK

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SIPDIS

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SUBJECT: NORTH-SOUTH FOREX TRANSFER DISPUTE CONTINUES

REF: KHARTOUM 1034

¶1. (SBU) In a September 25 meeting with CDA Fernandez, Central Bank of Sudan (CBOS) Governor Dr. Sabir Mohamed Hassan asserted that the Bank of Southern Sudan's (BOSS) refusal to transfer excess foreign currency reserves to Khartoum was a clear violation of the CPA that was hampering his ability to conduct a unified monetary policy and manage the country's exchange rate. He blamed political interference from GOSS leaders on his deteriorating relationship with his Deputy, BOSS President Elijah Malok Aleng Mayen, and implored CDA Fernandez to urge GOSS leaders to refrain from politicizing monetary issues. Hassan also requested CDA's assistance in protecting CBOS assets frozen at the Federal Reserve Bank of New York from a U.S. federal court ruling ordering the GOS to pay compensation to the families of US sailors killed in the 2000 terrorist attack on the USS Cole in Yemen. CDA Fernandez noted that the U.S. Judiciary is independent from the Executive branch, but suggested that a meeting between the Sudanese Embassy in Washington and the US Treasury Department might be helpful in clarifying the issues. End Summary.

¶2. (SBU) Hassan began by stating that the Comprehensive Peace Agreement (CPA) is very clear on matters related to the CBOS and the conduct of monetary policy, in no small part due to his insistence that such details be spelled out during negotiations in Navaisha. (Note: Hassan, who holds a Ph.D. in Economics from Syracuse University and is a veteran of the IMF in Washington, is widely viewed as an able technocrat. End Note.) He stated that the CBOS has autonomy and independence to pursue a unified monetary policy. "The CPA is very clear in stating the unity of the Central Bank," said Hassan, adding that the BOSS is a branch of the CBOS and its Deputy, Elijah Malok Aleng Mayen, is subordinate and accountable to him. (Note: The SPLM's longstanding position is that the BOSS is merely a "second window" of the CBOS and not a subordinate entity. End Note.)

¶3. (SBU) The ongoing dispute, stated Hassan, centers around the management of foreign exchange reserves (Reftel). The CPA is very clear with regard to the unity of foreign exchange reserves, he said, explaining that foreign exchange does not "belong" to the CBOS per se but rather to the economy as a whole. The CBOS is merely the custodian, and as such it is responsible for availing foreign exchange to the national economy. "Whoever needs foreign exchange comes to the CBOS," he said. The CBOS acquires foreign exchange from both the government and the private sector by buying it through local currency, and vice versa. The management of foreign exchange reserves is the purview of the CBOS Board of Directors, he said, and the policy is two-pronged. (Note: BoSS President Elijah Malok is a member of the CBOS Board of Directors. End note.) First, he noted, a working balance of foreign exchange is made available for the economy. Second, excess reserves are innvested. To implement this policy, he said, the CBOS has a window in Khartoum as well as in Juba. If there is a drop in the working balance of foreign exchange, the excess is pooled and redistributed. "This process is managed by

the CBOS," he said.

¶4. (SBU) Starting last December, however, the GOSS instructed the BOSS to halt transfer of foreign exchange reserves to the North, claiming they belonged to the South. Hassan strongly denied the claim, explaining how these reserves were already exchanged for local currency by the CBOS. "They can't have their cake and eat it too," he said. After several months of wrangling, the GOSS eventually relented because "they had no counterarguments," noted Hassan. But despite acknowledging that all foreign exchange reserves were in the purview of the CBOS, they insisted that those held in the South remain at the BOSS in Juba. "I told them that any excess reserves must be transferred to the CBOS for investment, but they refused," he said.

¶5. (SBU) In response to the South's actions, Hassan stated that he began withholding local currency from the South pending transfer of the excess reserves. This prompted an outcry from the South, and following intervention by Salva Kiir, Hassan stated that he was compelled by the Presidency to resume local currency transfers. But the situation has continued, and excess reserves in the South have accumulated to a substantial amount, he said, noting that the lack of control of all of Sudan's foreign exchange reserves impedes his ability conduct a unified monetary policy and manage the country's exchange rate. "You can't have two places managing monetary policy," he said.

¶6. (SBU) Hassan stated that he wrote a letter to Aleng requesting a transfer of excess reserves to the CBOS in Khartoum, which was met with no response. A reminder was similarly ignored, so he resorted to withholding the hard currency share of the South's oil revenue shares in favor of local currency. "They are protesting, claiming

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that I'm withholding their share of the proceeds, while I'm in fact deducting it from money owed," he said.

¶7. (SBU) Hassan stated that he expressed disappointment to Aleng that politics were interfering with the conduct of monetary policy. "Our past successes were based on the lack of political interference in our operations," he said. "Now, the GOSS is politicizing issues which should not be politicized. Hassan implored CDA Fernandez to advise the GOSS to stay out of monetary affairs. "Let us wait until 2011, but until then we all must abide by the rules," he said.

¶8. (SBU) Hassan also requested the assistance of CDA Fernandez in protecting the CBOS assets frozen at the Federal Reserve Bank of New York from a U.S. federal court ruling ordering the GOS to pay compensation to the families of US sailors killed in the 2000 terrorist attack on the USS Cole in Yemen. "The lawsuit is politically motivated, and the Central Bank has nothing to do with it," he lamented. CDA Fernandez agreed that it has nothing to do with the Central Bank, but noted that the U.S. Judiciary is independent from the Executive branch. He suggested that a meeting between the Sudanese Embassy in Washington and the US Treasury might be beneficial and that the State Department could try to facilitate such a meeting so that the Sudanese would at least have a better understanding of the issue.

¶10. (SBU) Comment: Hassan presents himself as an apolitical technocrat, and in fact he is widely recognized by the international community in Khartoum for his commitment to both the letter and spirit of the CPA and his handling of the current row reflects this. The fact that the current dispute grew out of the December 2007 cabinet crisis between the NCP and the SPLM indicates that it is likely entirely political, and as such a political solution is the best hope for resolving it. The GOSS, after two years of inconsistent support from the GNU on its hard currency needs, has pegged the stockpiling of currency in foreign banks to an evolving "day after" 2011 independence referendum strategy. The GNU, concerned that the GOSS may take a page from its own playbook, lacks confidence that its request for hard currency will be honored from its partners in the south. The entire dispute holds little space for compromise, and the GOSS sees the foreign currency issue as a "sovereign" one for the South to manage (reftel.) The GOSS also has liquidity issues that may prevent it from transferring the money.

Therefore it is unlikely the BOSS will agree to transfer the money, gambling that Khartoum will not fall on its sword over the issue. However the GOSS is on thin ice in terms of CPA prerogatives as defined between the Government of National Unity and the Government of Southern Sudan. Over time this is yet another issue that irritates relations between the parties and can be held up as an excuse for not implementing other parts of the CPA. It is one where the letter of the agreement favors Khartoum while political considerations - the South's fear and suspicions of Khartoum's intentions - trump any effort by the GOSS to fulfill their side of this portion of the peace accord.

FERNANDEZ